

110 FERC ¶ 61,164
UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Pat Wood, III, Chairman;
Nora Mead Brownell, Joseph T. Kelliher,
and Suedeem G. Kelly.

Midwest Independent Transmission System Operator, Docket Nos. ER04-1160-000
Inc. . ER04-1160-001

ORDER ACCEPTING NOTICE OF WITHDRAWAL, CONDITIONALLY
ACCEPTING PROPOSED TARIFF REVISIONS,
AND DIRECTING COMPLIANCE FILING

(Issued February 16, 2005)

1. In this order, we conditionally accept for filing, to be effective October 30, 2004, as requested, proposed revisions to the limitation of liability provisions of Midwest Independent Transmission System Operator, Inc.'s (Midwest ISO) Open Access Transmission Tariff (OATT), submitted for filing by Midwest ISO and American Transmission Company LLC (ATCLLC) (collectively, Applicants). We also accept the proposed Notice of Withdrawal of the proposed revisions to the indemnification provision of the Midwest ISO OATT. We also direct Applicants to submit a compliance filing.

2. This order is consistent with the Commission's efforts to facilitate the development of regional transmission organizations (RTOs) in order to benefit all customers.

I. Background

3. The current limitation of liability provisions in the Midwest ISO OATT have been in effect since August 5, 2002.¹ The provisions hold Midwest ISO and its Transmission Owners liable for any act or omission that results in an interruption, deficiency or imperfection of service in cases of ordinary negligence, gross negligence, and intentional misconduct. However, recovery of indirect or consequential damages is precluded under any circumstance, *i.e.*, Midwest ISO and its Transmission Owners are liable for only direct damages.

¹ See *Midwest Independent Transmission System Operator, Inc.*, 100 FERC ¶ 61,144 (2002) (August Order).

4. In the August Order, the Commission noted that it was considering the issue of limited liability as part of its ongoing effort to harmonize wholesale power markets in the context of the new realities of regional electricity markets.² At that time, this effort included a generic rulemaking proceeding regarding open access transmission service and standard market design (SMD NOPR),³ and one of the issues on which comment was sought was whether a new open access transmission tariff should include standardized provisions that limit the liability of Independent System Operators (ISOs), RTOs, and the transmission owners whose facilities these ISOs or RTOs control. While the SMD NOPR and a subsequent White Paper⁴ associated with the SMD NOPR addressed liability issues, neither included substantive discussion of indemnification issues.

II. Proposed Tariff Revisions

5. On August 30, 2004, Applicants filed proposed revisions to sections 10.2 (Indemnification), 10.3 (Limitation of Liability), 10.4 (Direct Damages) and 10.5 (Inclusion of Independent Transmission Companies) of Midwest ISO's OATT. The proposed revisions provide that Midwest ISO and its Transmission Owners will not be liable to transmission customers, users or other third parties or persons for any damages in cases of ordinary negligence associated with service provided under the Midwest ISO OATT. In addition, Midwest ISO and Transmission Owners would be liable for only direct damages in cases of gross negligence or intentional misconduct.

6. More specifically, the proposed section 10.3, Limitation of Liability, would provide, in pertinent part:

(a) The Transmission Owner shall not be liable, whether based on contract, indemnification, warranty, tort, strict liability or otherwise, to any Transmission Customer, User or any third party or other person for any damages whatsoever, including, without limitation, direct, incidental, consequential, punitive, special, exemplary or indirect damages arising or resulting from any act or omission in any way associated with service provided under this Tariff . . . except to the extent that the Transmission Owner is found liable for gross negligence or intentional misconduct, in which case the

² See August Order at P 24.

³ *Remedying Undue Discrimination through Open Access Transmission Service and Standard Market Design, Notice of Proposed Rulemaking*, FERC Stats. & Regs. ¶ 32,563 (2002).

⁴ *Remedying Undue Discrimination through Open Access Transmission Service and Standard Market Design, Notice of White Paper*, Docket No. RM01-12-000 (Apr. 28, 2003) (White Paper).

Transmission Owner will only be liable for direct damages. Nothing in this section, however, is intended to affect obligations otherwise provided in agreements between the Transmission Provider and Transmission Owner.

(b) The Transmission Provider shall not be liable, whether based on contract, indemnification, warranty, tort, strict liability or otherwise, to any Transmission Customer, User or any third party or other person for any damages whatsoever, including, without limitation, direct, incidental, consequential, punitive, special, exemplary or indirect damages arising or resulting from any act or omission ... associated with service provided under this Tariff, . . . except to the extent that the Transmission Provider is found liable for gross negligence or intentional misconduct, in which case the Transmission Provider will only be liable for direct damages.

(c) Neither the Transmission Owner nor the Transmission Provider shall be liable for damages arising out of services provided under this Tariff . . . occurring as a result of conditions or circumstances beyond the control of the Transmission Owner or Transmission Provider . . . or resulting from electric system design . . . or electric system operation practices or conditions common to the domestic electric utility industry. Transmission Owner shall not be liable for acts or omissions done in compliance or good faith attempts to comply with directives of Transmission Provider.

7. Similarly, in revised section 10.5, Applicants propose to extend limited liability protection to owners and operators of generation facilities, who act in good faith in implementing Midwest ISO's directives.⁵

⁵ Proposed section 10.5, Inclusion of Independent Transmission Companies, states:

For purposes of sections 10.3 and 10.4 above, independent transmission companies under Appendix I of the ISO Agreement shall be included in the definition of "Transmission Owner" as used therein and such limitations of liability and damages shall be applicable to those entities. In addition, the limitations of liability and damages set forth in sections 10.3 and 10.4 shall be applicable to owners and/or operators of generating facilities acting in good faith to implement or comply with the directives of the Transmission Provider.

8. And in the revised section 10.4, Applicants propose to define “direct damages” to exclude certain types of losses.⁶

9. Applicants propose to modify the Midwest ISO OATT because RTOs, ISOs, and stand-alone transmission companies, now solely regulated by the Commission, are not protected by liability provisions available to state-regulated, bundled retail service providers. Applicants assert that state-regulated utilities are routinely protected from liability for their ordinary negligence and that the same level of protection should be afforded to wholly federally-regulated public utilities.⁷

10. Applicants point to the SMD NOPR, the White Paper, and the 2004 Reliability Policy Statement⁸ as evidence that the Midwest ISO’s OATT should be revised to provide broader liability protection. Although the Midwest ISO OATT currently contains some limitation of liability provisions, Applicants assert that these provisions are not entirely consistent with the White Paper, to the extent that Midwest ISO and Transmission Owners may be held liable for direct damages arising out of ordinary negligence. Applicants further note that the current Midwest ISO OATT affords no protection to owners or operators of generation facilities acting in good faith to implement Midwest ISO’s directives.

11. Applicants also argue that the revisions proposed here are distinct from the liability issues set for settlement judge procedures in the Commission’s order conditionally accepting Midwest ISO’s Open Access Transmission and Energy Markets Tariff (TEMT).⁹ Applicants state that the provisions at issue in that proceeding would be included in the Transmission Owners agreement or a similar agreement between Midwest ISO and Transmission Owners/Control Area Operators, while the instant filing relates solely to liability arising out of services provided under Midwest ISO’s OATT.

⁶ Under proposed section 10.4, Direct Damages shall not include: damages relating to loss of profit, loss of revenue, loss of production, loss of earnings, loss of contract, loss of use of equipment, cost of capital, cost of temporary equipment or services, or any other incidental, punitive, exemplary, indirect, special or consequential loss or damage.

⁷ See Transmittal Letter I at 6, n.24.

⁸ See *Policy Statement on Matters Related to Bulk Power System Reliability*, 107 FERC ¶ 61,052 (April 19, 2004) (2004 Reliability Policy Statement).

⁹ See *Midwest Independent Transmission System Operator, Inc.*, 108 FERC ¶ 61,163 (2004) (August 6 Order).

12. Applicants argue that inadequate liability protection could adversely affect Midwest ISO's ability to fulfill its function as a transmission provider in three areas. First, Applicants assert that inadequate liability protection leads to higher insurance, finance and litigation costs arising out of liability that extends to ordinary negligence and that these costs may lead to higher transmission rates. Second, they assert that inadequate liability protection may discourage utilities from transferring ownership or control of assets to Midwest ISO or stand-alone transmission companies, thus adversely affecting the Commission's efforts to restructure the electricity industry. Third, they assert that potential damages associated with liability for ordinary negligence, even when limited to direct damages, are significant, and could force Midwest ISO to consider liquidation in a bankruptcy proceeding.

13. In addition, Applicants sought to revise the indemnification provision of the Midwest ISO OATT (section 10.2) to provide that transmission customers will indemnify Midwest ISO and its Transmission Owners against costs and liabilities by or to third parties, except in cases of gross negligence or intentional wrongdoing. A deficiency letter issued on October 28, 2004 requested, among other things, clarification of issues raised by the proposed revisions to the Midwest ISO OATT's indemnification provisions. In response to the deficiency letter, Applicants made a supplemental filing on November 24, 2004. The supplemental filing, among other things, included a Notice of Withdrawal of the proposed Second Revised Sheet No. 49 that contained the proposed revised section 10.2 of the OATT.

14. Applicants request an effective date of October 30, 2004.

III. Notice of Filing, Interventions, and Protests

15. Notice of Applicants' filing was published in the *Federal Register*, 69 Fed. Reg. 54,665 (2004), with comments, protests or interventions due on or before September 20, 2004. Notice of the supplemental filing was published in the *Federal Register*, 69 Fed. Reg. 70,438 (2004), with comments, protests or interventions due on or before December 7, 2004.

16. Wisconsin Electric Power Company filed a timely motion to intervene. Timely motions to intervene and comments in support of the proposed revisions were filed by the Midwest ISO Transmission Owners and the Midwest Stand-Alone Transmission Companies (MSATs).¹⁰ Duke Energy North America, LLC and Duke Energy Trading and Marketing, LLC (collectively, Duke Companies); the Michigan Public Power

¹⁰ MSATs include GridAmerica LLC (GridAmerica), International Transmission Company (IT), and Michigan Electric Transmission Company, LLC (METC). METC is a Transmission Owner member of Midwest ISO. GridAmerica and IT are Independent Transmission Companies (ITCs) under Appendix I of the Midwest ISO Agreement.

Agency and the Michigan South Central Power Agency (collectively, Michigan Agencies), WPS Resources Corporation (WPSR),¹¹ and the Coalition of Midwest Transmission Customers (CMTC)¹² filed timely motions to intervene with protests. Consumers Energy Company (Consumers) filed a motion to intervene that generally supported the proposed revisions but sought clarification on certain issues.

17. Motions to intervene out-of-time were filed by Great River Energy (Great River) and Wolverine Power Supply Cooperative (Wolverine).

18. On October 5, 2004, Applicants filed an answer to the protests.

19. CMTC filed comments that support the withdrawal of the proposed Second Revised Sheet No. 49.

IV. Discussion

Procedural Matters

20. Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.214 (2004), the timely, unopposed motions to intervene serve to make the entities that filed them parties to this proceeding. We will grant Great River's and Wolverine's motions to intervene out-of-time given their interests in this proceeding, the early stage of this proceeding, and the absence of any undue prejudice or delay.

21. Rule 213(a)(2) of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.213(a)(2) (2004), prohibits an answer to a protest unless otherwise ordered by the decisional authority. We will accept Applicants' answer because it has provided information that assisted us in our decision-making process.

Intervenor Comments

22. The Midwest ISO Transmission Owners and MSATs echo the reasoning set forth by Applicants in support of the proposed revisions. They argue that the proposed revisions would: (1) ensure that Midwest ISO's liability standards are consistent with

¹¹ WPSR filed the motion to intervene and comments on behalf of Wisconsin Public Service Corporation, Upper Peninsula Power Company, WPS Power Development Inc., and WPS Energy Services Inc.

¹² CMTC is an *ad hoc* group of large industrial end-users of electricity. All CMTC members operate one or more manufacturing facilities in the Midwest and purchase electric delivery service or bundled electric service from at least one of Midwest ISO's Transmission Owners.

those used by other RTOs; (2) enable Midwest ISO and facility owners to better manage insurance premiums; (3) more closely track liability protections generally available under state law; (4) make the ownership of jurisdictional facilities and participation in jurisdictional RTOs more attractive; and (5) afford a measure of protection against uncertain and potentially disastrous damage awards.

23. Duke Companies, Consumers and WPSR do not generally oppose the proposed revisions. While Duke Companies articulate their full support of the filing, these parties seek certain clarifications or modifications. Duke Companies seek extension of the indemnification provisions in section 10.2 to operators of generating facilities acting in good faith to implement the directives of Midwest ISO, consistent with the extension of the limited liability provisions to such generators in proposed section 10.5. Consumers requests that the Commission clarify that the proposed revisions will not affect or negate the liability provisions contained in bilateral agreements already on file with the Commission. More specifically, it seeks assurance that the proposed revisions will not apply to the Distribution-Transmission Interconnection Agreement between it and Michigan Electric Transmission Company, LLC (METC). WPSR sees a potential conflict between the liability provisions proposed here and those at issue with regard to Midwest ISO's Energy Market Tariff. WPSR requests that the Commission clarify that the proposed revisions apply to transmission-only services and would not address issues concerning liability protection for market or control area operation-related services that are currently being addressed in the settlement discussions on the allocation of functions between Midwest ISO and control areas directed by the Commission in the August 6 Order.¹³

24. While the Michigan Agencies do not categorically oppose the concept of limiting recovery to direct damages, they assert that the proposed revisions were not vetted through the stakeholder process and should therefore be rejected. They also object to the proposed definition of "Direct Damages," which they claim is ambiguous.¹⁴ They assert that the proposed definition is unnecessary because the concept of direct and consequential damages has been well-defined by the courts within various jurisdictions.

¹³ See August 6 Order at P 137-38.

¹⁴ Proposed section 10.4, Direct Damages, states:

As used herein, direct damages shall not include damages relating to loss of profit, loss of revenue, loss of production, loss of earnings, loss of contract, loss of the use of equipment, cost of capital, cost of temporary equipment or services, or any other incidental, punitive, exemplary, indirect, special or consequential loss or damage.

25. CMTC urges the Commission to reject the proposed revisions to the tariff liability limitation provisions. It argues that, although the White Paper reflects the Commission's initial intention to establish a standardized limitation on liability for transmission providers, a final rule has not yet issued. CMTC further argues that, while the Commission accepted similar liability provisions for RTO-NE,¹⁵ that proceeding is ongoing and does not establish precedent for the filing here. CMTC further asserts that the Commission has clarified that, because the issue of limited liability has not been resolved, it will consider limited liability provisions on a case-by-case basis. CMTC also contends that the proposed tariff revisions are unnecessary to encourage participation in Midwest ISO, or reflect the risks associated with RTO participation, because the 12.88 percent return on equity currently allowed Transmission Owners under the formula transmission rate in Attachment O of the Midwest ISO OATT achieves these purposes. CMTC asserts that, upon joining Midwest ISO, Transmission Owners were aware of the current liability provisions in the Midwest ISO OATT and that revising those provisions as proposed here would lead to a double-recovery of costs. CMTC further argues that the "built-in protections of the legal process" will protect Applicants from unlimited damage awards.¹⁶ CMTC states that the costs associated with negligence will be passed through to customers, thereby easing the burden on Midwest ISO and Transmission Owners.

Applicants' Response

26. In response to WPSR, Applicants argue that, because the TEMT will completely replace the Midwest ISO OATT on March 1, 2005, Midwest ISO intends to update the TEMT liability limitation provisions with the language accepted by the Commission in this case. Applicants argue that, contrary to WPSR's concerns, there will not be a conflict between the revisions proposed here and the liability provisions at issue in the settlement discussions (directed by the Commission in the August 6 Order) on the allocation of functions between Midwest ISO and control areas. They state that the proposed limited liability provisions would apply to Transmission Owners (including ITCs) and Midwest ISO as to the provision of transmission service and actions taken by generators at the direction of Midwest ISO, while liability issues in the settlement discussions would apply to Balancing Authorities as to their functions. Applicants submit that, whether the current or proposed liability provisions should apply to control area operators or Balancing Authorities is a policy issue that the Commission can decide when and if it is raised concerning a settlement agreement on the allocation of functions between Midwest ISO and control areas.

27. In response to Michigan Agencies, Applicants argue that the proposed revisions were in fact vetted through the stakeholder process. Applicants state that the filing was distributed to the Midwest ISO Tariff Working Group more than two weeks before the

¹⁵ See *ISO New England, et al.*, 106 FERC ¶ 61,280 (2004), *reh'g pending*.

¹⁶ See CMTC Protest at 11.

filing was made and that they received no comments on the proposed tariff changes. In addition, Applicants state that the filing was listed as a discussion item on Midwest ISO's August Advisory Committee Meeting Agenda, the filing was presented at that meeting, which was widely attended, and no one voiced opposition.

Commission Determination

28. We will accept the unopposed Notice of Withdrawal of proposed revisions to the tariff indemnification provisions in Second Revised Sheet No. 49.

29. We will conditionally accept the proposed limitation of liability provisions, to become effective October 30, 2004, as requested. As noted by the United States Court of Appeals for the District of Columbia Circuit, prior to unbundling many state commissions had approved retail tariff provisions permitting utilities to limit their liability for service interruptions to instances of gross negligence or willful misconduct.¹⁷ Courts found that such provisions balance lower rates for all customers against the burden of limited recovery for some, and that the technological complexity of modern utility systems and resulting potential for service failures unrelated to human errors justify liability limitations.¹⁸ We agree. Midwest ISO and stand-alone transmission companies are solely regulated by the Commission for their provision of transmission services, so the Commission is the only regulator with the ability to ensure that they are protected from potentially excessive damage awards by adequate limitation of liability provisions. Many state commissions in the Midwest ISO footprint have traditionally allowed, and continue to allow, utilities to limit their liability to gross negligence.¹⁹ We believe that Midwest ISO and its Transmission Owners should be afforded similar protection. Otherwise, disparate treatment is a disincentive to participate in Midwest ISO.²⁰

¹⁷ *Transmission Access Policy Study Group v. FERC*, 225 F.3d 667, 727 (D.C. Cir. 2000).

¹⁸ *Id.*

¹⁹ In response to the deficiency letter, Applicants provided the currently effective limitation of liability provisions in the state-regulated, retail tariffs of the Midwest ISO Transmission Owners and the state-regulated utilities that formerly owned or operated transmission facilities that are now owned and/or operated by stand-alone transmission companies in Midwest ISO. Applicants indicated in their response that more than half of the currently effective state liability provisions provide liability protection with a gross negligence standard or simply provide for "no liability" without additional specification.

²⁰ As we noted in the August Order at P 24, limitation of liability provisions are also important where there is no liability protection under state law.

30. As we stated earlier, without adequate limitation of liability provisions, Midwest ISO and its Transmission Owners would be exposed to potentially excessive damage awards. We agree with Applicants that such risk would also be reflected in higher insurance premiums (to the extent that adequate liability coverage is even available) and higher cost of capital, which, in turn, would be borne by customers and could result in inequities among customers.

31. Midwest ISO and Transmission Owners must provide service to all eligible customers, and cannot deny service to particular customers based on the risk of potential damages associated with interruption of service to those customers. Nor can they easily quantify the potential risk associated with service to such customers and price such service accordingly. Therefore, all customers would ultimately bear the cost associated with the risk of such service, including those customers that do not have special reliability needs.

32. CMTC argues that the proposed revisions are unnecessary because there are “built-in protections” in the legal system, which will allow damage awards to be passed through to customers, thereby diluting the financial impact to the transmission provider. However, it is precisely because excessive damage awards may be passed through to customers, through increased rates, that we believe strong limitation of liability provisions are needed. Such provisions will help minimize the financial impact they ultimately bear.

33. CMTC argues that the proposed revisions are unnecessary to encourage investment, given the 12.88 percent return on equity in the formula transmission rates in the Midwest ISO OATT. It also argues that this return on equity already compensates Transmission Owners for risks associated with existing liability provisions in the Midwest ISO OATT, so that revising those provisions as proposed here would lead to a double-recovery of costs. However, CMTC has not disputed that limitation of liability provisions are just one of many factors that impact a company’s cost of capital. In fact, a number of factors have a bearing on utilities’ cost of capital, not just liability risks, and CMTC has provided no information or analysis showing that the 12.88 percent return on equity in the Midwest ISO OATT is driven entirely or even significantly by limitation of liability provisions.

34. We further agree with Applicants’ proposed revisions to section 10.5, which provide that owners and operators of generation facilities acting in good faith to implement Midwest ISO’s directives should be extended the same limitation of liability protection afforded to Midwest ISO and the Transmission Owners in sections 10.3 and 10.4. We also agree with Duke Companies that the reasons for extending liability protection to owners and operators of generation facilities apply equally to extending the indemnification protections set forth in the Midwest ISO OATT. We see no reason to grant such generators liability protection but exclude such generators from indemnification protections. Accordingly, just as the Applicants have extended liability

protection in section 10.5, we will direct Applicants similarly to extend indemnification protection in section 10.5. Applicants are directed to submit a compliance filing, within 30 days of the date of this order, modifying section 10.5, to extend the indemnification protections (set forth in section 10.2) to owners and operators of generating facilities acting in good faith to implement the directives of Midwest ISO.

35. We will direct Applicants to submit a compliance filing, within 30 days of the date of this order, deleting the definition of “Direct Damages” from section 10.4. We agree with Michigan Agencies that the proposed definition is ambiguous and, contrary to Applicants’ contention, we do not believe that the proposed definition will prevent unnecessary litigation over what constitutes direct damages. That question is one for the courts, who are familiar with the concepts of direct and consequential damages.

36. Further, we agree with Consumers’ argument that the proposed revisions should not negate liability provisions in existing agreements. In conditionally accepting the proposed revisions, we do not intend to abrogate any existing agreements. In order to provide clarification on this issue, we will direct Applicants to submit a compliance filing, within 30 days of the date of this order, modifying proposed section 10.3 to specifically provide that those sections shall not affect responsibilities otherwise provided for in agreements among the parties predating the effective date of the current revisions, *i.e.*, October 30, 2004.

37. WPSR requests clarification that the proposed tariff revisions will not create a conflict with the liability provisions at issue in the settlement discussions on the allocation of functions between Midwest ISO and control areas. Parties to those negotiations filed an offer of settlement on October 5, 2004. The proposed tariff provisions conditionally accepted here address the liability of Midwest ISO and Transmission Owners for service provided under the Midwest ISO OATT, effective October 30, 2004, while the liability provisions in the offer of settlement address liability of Midwest ISO and Balancing Authorities once Midwest ISO’s TEMT takes effect (scheduled to occur on March 1, 2005). Midwest ISO has committed to file to update the TEMT before it takes effect to incorporate the language accepted herein. To the extent that concerns regarding conflicts between the proposed tariff revisions conditionally accepted here and those contained in the offer of settlement still remain at the time Midwest ISO makes that filing, such concerns are more appropriately addressed in that proceeding or in settlement proceeding that is pending before the Commission.

38. Finally, we are not persuaded by Michigan Agencies’ argument that the proposed revisions should be rejected because they were not vetted through the stakeholder process. We are satisfied by Applicants’ response that, prior to filing, the proposed revisions were presented to stakeholders on two separate occasions and no party voiced opposition to the revisions.

The Commission orders:

(A) Applicants' Notice of Withdrawal of proposed Second Revised Sheet No. 49 is hereby accepted.

(B) Applicants' proposed tariff revisions are hereby conditionally accepted for filing, to become effective October 30, 2004, subject to Ordering Paragraph (C) below.

(C) Applicants are hereby directed to submit a compliance filing, within 30 days of the date of this order, as discussed in the body of this order.

By the Commission. Commissioner Kelly dissenting with a separate statement to be issued later.

(S E A L)

Magalie R. Salas,
Secretary.